

Internal Revenue Service

Department of the Treasury

**District
Director**

1100 Commerce St., Dallas, Texas 75202

Date: OCT 23 1995

Employer ID Number:

Person to Contact:

Telephone Number:

Refer Reply To:

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under section 501(c)(4) of the Internal Revenue Code.

The information submitted indicates that you incorporated in the State of [REDACTED] on [REDACTED]. Article IV of your Articles of Incorporation states that your specific purpose is to provide maintenance, preservation and architectural control of the residential lots, townhouses, and all common facilities and properties within those certain tracts of property shown to be included within a subdivision in [REDACTED] County, [REDACTED], known as [REDACTED]. Article IV also states that your purpose is to promote the recreation, health, safety and welfare of your residents.

Article 2 of your Bylaws states that each person occupying and acquiring record title to a fee or undivided fee interest in any lot or townhouse within [REDACTED] shall be a member of your Association.

You are formed to provide for the recreation, health, safety and welfare of [REDACTED]. You are within the boundaries of [REDACTED] District. You are comprised of [REDACTED] parcels with [REDACTED] occupied residences and an estimated population of [REDACTED]. Your activities include the following:

1. The maintenance of esplanades, entrances, roadsides and mowing/landscaping of common areas;
2. Pest and mosquito control;
3. Providing law enforcement;
4. Providing streetlights on all public roads within your jurisdiction;
5. Maintenance of hike/bike trails;
6. Management and deed restriction enforcement.

The mosquito spraying is done throughout the entire subdivision area. You

contract with a management company to monitor and enforce deed restrictions.

Your primary source of financial income is member assessments. Your expenses include the following:

Expense category

Security

\$

\$

\$

Pest Control

As of , you had a total fund balance or net assets of \$. Your cash balance as of was \$. You have incurred excess revenues each year as follows:

Year

Excess Revenue

\$

A newsletter provided with your 1024 application indicates that is located within your boundaries. This club is an independent club with private membership.

Your correspondence dated states the following:

- owns ;
- The annual assessment is \$ per member. Certain sections of your association are assessed an additional amount to cover their prorata expenses incurred for landscaping and yard maintenance. The additional assessment is based on the actual costs incurred;
- The hike and bike trail has no restrictions to the general public;
- Your members are not required to belong to the .

A map of your area was included with this correspondence. It shows that there is a courthouse, library and two schools in your area. However, it could not be determined whether these are within your boundaries since the boundaries to your association were not on this map.

A copy of your agreement with County was provided with this correspondence. This agreement calls for the Constable, Precinct of County to provide you with one extra deputy. You have agreed to pay County the sum of \$ for providing the extra deputy for the 12 month period beginning .

A copy of the Reservations, Restrictions and Covenants was also provided with this correspondence. Section 1 of Article III of this document states that no building shall be erected, altered or permitted to remain on any lot other than one detached single-family residential dwelling. Section 5 of Article III of this document states that no lot in the subdivision shall be used for any commercial business or professional purpose nor for church

purposes. There are seven additional sets of Declaration of Covenants, Conditions and Restrictions for other sections of your association, which were not provided. These additional Declarations are very similar in nature to the one provided.

Your correspondence dated [REDACTED] states the following:

- The additional assessments to your members to cover their prorata share of the expenses incurred for the landscaping and yard maintenance of their lots are as follows:

<u>Year</u>	<u>Additional assessment</u>
[REDACTED]	\$ [REDACTED]

- Your miscellaneous revenue are reimbursements. The security reimbursement is the prorated amount from a neighboring subdivision that shares in the [REDACTED] County Constable contract with [REDACTED];
- Your association consists of [REDACTED] acres;
- The income and expense breakdown for the year ending [REDACTED] was provided. It shows that your security expense for the year totaled \$[REDACTED]. Your excess revenue over expenses for the year totaled \$[REDACTED];
- You provide numerous city-like and government-like services such as law enforcement, streetlights, maintenance and mosquito fogging;
- You do not maintain the exterior of any residential structures;
- All of your common areas and facilities are open to the general public.

Section 501(c) of the Code describes certain organizations exempt from Federal income tax under section 501(a) and reads, in part, as follows:

"(4) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes."

Section 1.501(c)(4)-1 of the regulations provides, in part, as follows:

"(a)(1) In general. A civic league or organization may be exempt as an organization described in section 501(c)(4) if -

(i) It is not organized or operated for profit; and

(ii) It is operated exclusively for the promotion of social welfare."

"(a)(2)(i) An organization is operated exclusively for the promotion of social welfare when it is primarily engaged in promoting, in some way, the common good and general welfare of the people of the community. An organization embraced within this section is one which is operated primarily for the purpose of

bringing about civic betterments and social improvements *** The promotion of social welfare does not include direct or indirect participation or intervention in political campaigns on behalf of or in opposition to any candidate for public office. Nor is an organization operated primarily for the promotion of social welfare if its primary activity is operating a social club for the benefit, pleasure, or recreation of its members, or is carrying on a business with the general public in a manner similar to organizations which are operated for profit.***"

Revenue Ruling 69-280, 1969-1 C.B. 152, describes a nonprofit organization formed to provide maintenance of the exterior walls and roofs of homes of members who own houses in a development. The services include the painting of exterior walls and repair of roofs. If a person purchases a unit in the housing development, he is required to become a member of the organization. The organization is not exempt as a social welfare organization under section 501(c)(4).

Revenue Ruling 72-102, 1972-1 C.B. 149, describes an organization formed by a developer to preserve the appearance of a housing development and to maintain streets, sidewalks and common areas for the use of the residents, which was found to be exempt under Internal Revenue Code section 501(c)(4). The rationale behind this decision was that the organization served the common good and general welfare of the entire community because it owned and maintained certain non-residential, non-commercial properties of the type normally owned and maintained by municipal governments. Administering and enforcing covenants for preserving the architecture and appearance of a housing development was incidental to the overriding public benefit.

Revenue Ruling 74-99, 1974-1 C.B. 131, modified Revenue Ruling 72-102. It provides that in order to qualify for exemption under IRC 501(c)(4), a homeowners' association: must serve a "community" which bears a reasonable recognizable relation to an area ordinarily identified as governmental; must not conduct activities directed to the exterior maintenance of private residences; and the common areas or facilities it owns and maintains must be for the use and enjoyment of the general public. According to this revenue ruling, a community within the meaning of section 501(c)(4) is not simply an aggregation of homeowners bound together in a structured unit formed as an integral part of a plan for the development of a real estate subdivision and the sale and purchase of homes therein. The term "community" as used in section 501(c)(4) has traditionally been construed as having reference to a geographical unit bearing a reasonably recognizable relationship to an area ordinarily identified as a governmental subdivision or a unit or district thereof. The revenue ruling was intended only to approve ownership and maintenance by a homeowners' association of such areas as roadways and parklands, sidewalks, and street lights, access to, or the use and enjoyment of which is extended to members of the general public, as distinguished from controlled use or access restricted to the members of the homeowners' association.

According to Revenue Ruling 80-63, 1980-1 C.B. 116, no hard and fast rule can be applied as to what constitutes a "community," but each case must be examined to determine whether the activities of the organization have sufficient community benefit to serve a social welfare purpose under IRC 501(c)(4). Although the area represented by an association may not be a community, if the association's activities benefit a community, it may still qualify for exemption. For instance, if the association owns and maintains common areas and facilities for

the use and enjoyment of the general public as distinguished from areas and facilities whose use and enjoyment is controlled and restricted to members of the association, then it may satisfy the requirement of serving a community.

The Rancho Santa Fe Association v. U.S. court case involves Rancho Santa Fe, a large, self-contained housing development. The property contained in the development consists of 6,100 acres. The association has approximately 3,000 members. The association oversees the governance of the property within the development by enforcing the covenants and setting up various boards, including a planning board, a park board, a health board, a library board and recreation board. It also functions as a liaison between the community and the Board of Supervisors on issues which require the participation of larger governmental entities, such as maintenance of the rights-of-way and the sanitation system. Rancho Santa Fe has its own post office and zip code. Not all of the common areas and facilities the association owned and maintained were open to members of the general public for their use and enjoyment.

The development was found to be coextensive with the community it served, and therefore, the benefits bestowed by the association on the development benefit the general public within the requirements of statute. Exemption under section 501(c)(4) was recognized.

The Flat Top Lake Association, Inc. v. U.S. court case involves Flat Top Lake, a housing development. It maintains and operates a lake and other recreational facilities for the pleasure and convenience of its members. Flat Top Lake lacks certain indicia of a community such as churches, schools or stores. Entrance to the associations' property and use of its facilities is strictly limited to members and their guests. It has a sign on its entrance that states: "Flat Top Lake Association, Private Property, Members Only." The association does not meet the requirements of exemption set out in IRC 501(c)(4).

You are similar to the organization described in the Revenue Ruling 69-280. You are providing landscaping and yard maintenance services for your members private property. You are then assessing them for providing these services. Landscaping and yard maintenance can be considered the exterior maintenance of private residences.

You are not similar to the organization described in the Revenue Ruling 74-99 for the following reasons: (1) you are not a "community" which bears a reasonable recognizable relation to an area ordinarily identified as governmental; and (2) you conduct activities directed to the exterior maintenance of private residences. You are made up of single family residences. No lots in your subdivision shall be used for any commercial business or professional purpose nor for church purposes. Landscaping and lawn maintenance of your members private property can be considered exterior maintenance of private residences.

You are not similar to the organization described in the Revenue Ruling 80-63. You are not a community and your activities do not benefit a community. You are operated primarily for the private benefit of your members and any benefits to the community are not sufficient to meet the requirement that you be operated primarily for the common good and general welfare of the community. Security services which are in addition to those already provided and the landscaping and lawn maintenance of your members private property is for the private benefit of your members. These services do not benefit a community.

You are not similar to the Rancho Santa Fe Association because you are not a community. You have approximately [REDACTED] members and consist of [REDACTED] acres. Rancho Santa Fe has 3,000 members and consists of 6,100 acres. Rancho Santa Fe is a self-contained housing development. You are made up of single family residences.

You are similar to the Flat Top Lake Association. It is operated for the private benefit of its members. By providing security services and landscaping and lawn maintenance services for your members, you are operated primarily for their benefit.

You do not meet a basic requirement for exemption under section 501(c)(4) - that you operate in a non profit manner. The accumulation of \$[REDACTED] in fund balances or net assets, as well as consistently earning excess revenues clearly shows that you operate in a for profit manner.

Accordingly, it is held that you are not entitled to exemption from Federal income tax as an organization described in section 501(c)(4), and you are required to file Federal income tax returns on Form 1120.

As a homeowners' association, you may qualify for treatment under section 528. In this letter we are not ruling on the question of whether you qualify for treatment under section 528. However, if you believe you qualify for such treatment, you should file Form 1120-H when due.

If you do not agree with these conclusions, you may, within 30 days from the date of this letter, file in duplicate a brief of the facts, law, and argument that clearly sets forth your position. If you desire an oral discussion of the issue, please indicate this in your protest. The enclosed Publication 892 gives instructions for filing a protest.

If you do not file a protest with this office within 30 days of the date of this report or letter, this proposed determination will become final.

If you agree with these conclusions or do not wish to file a written protest, please sign and return Form 6018 in the enclosed self-addressed envelope as soon as possible.

If you have any further questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely,

[REDACTED]
District Director

Enclosures:
Publication 892
Form 6018